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TELEGRAM

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ACTION T-01

INFO CONG-01 CH-04 EP-02 P-01 RA-01 X-01 /010 A3 P8

INFO LOG-00 COPY-01 ADS-00 SS-00 EB-00 NSCE-00 SSO-00
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FM AMEMBASSY BEIJING
TO SECSTATE WASHDC IMMEDIATE 6534
INFO AMCONSUL SHANGHAI
AMCONSUL GUANGZHOU
AMCONSUL HONG KONG
AMCONSUL SHENYANG POUCH
AMCONSUL CHENGDU POUCH

CONFIDENTIAL BEIJING 35360

FOR P, T, EB/EWT, AND EAP/CH

E.O. 12356: DECL: OADR
TAGS: ETTC, ETRO, CH
SUBJECT: BACKGROUND STATEMENT ON U.S. EXPORT CONTROL
POLICY FOR CHINA

1. CONFIDENTIAL - ENTIRE TEXT.

2. SUMMARY AND ACTION REQUEST. U.S. STATEMENTS, PUBLIC AND PRIVATE, HAVE UNAMBIGUOUSLY DESCRIBED FOR CHINESE LEADERS THE INTENT AND SCOPE OF THE U.S. DECISION TO POSTPONE FURTHER LIBERALIZATION OF EXPORT CONTROLS FOR CHINA. SOME CHINESE PURCHASERS OF U.S. TECHNOLOGY, HOWEVER, REMAIN CONFUSED ABOUT THE FULL IMPLICATIONS OF OUR POLICY, WITH DETRIMENTAL EFFECTS FOR U.S. COMPETITIVENESS. IN ONE RECENT CASE, HEWLETT-PACKARD LOST A MAJOR CONTRACT IN PART DUE TO CHINESE FEARS THAT HP WOULD NO LONGER BE ABLE TO OBTAIN THE NECESSARY EXPORT LICENSE. HP BELIEVES ITS FRENCH COMPETITOR PLAYED ON CHINESE CONCERNS TO REVERSE AN EARLIER DECISION IN HP'S FAVOR AND WIN THE CONTRACT. U.S. BUSINESSMEN WERE RECOGNIZE THE REASONS THAT GUIDE U.S. EXPORT CONTROL POLICY, BUT ARE UNCERTAIN ABOUT THE INTENT OF THE ADMINISTRATION'S DECISION TO POSTPONE FURTHER LIBERALIZATION FOR THE TIME BEING. THEY ARE CONCERNED THAT THEY ARE BEING HURT BY MISINFORMATION OR A MISUNDERSTANDING SUGGESTING THAT THE U.S. HAS ROLLED BACK PREVIOUS LICENSING PROCEDURES AND APPROVAL LIMITS. TO COUNTERACT THIS, THE EMBASSY REQUESTS DEPARTMENT'S APPROVAL OF A BACKGROUND PAPER (SEE PARAGRAPH SEVEN BELOW), RESTATING U.S. EXPORT CONTROL POLICY FOR CHINA IN PREVIOUSLY-APPROVED LANGUAGE. END SUMMARY AND ACTION REQUEST.

3. THE ADMINISTRATION'S DECISION TO LINK FURTHER LIBERALIZATION OF TECHNOLOGY EXPORT CONTROLS ON CHINA TO EVIDENCE THAT THE PRC HAS CURBED ITS ARMS SALES TO IRAN HAS BEEN REPEATEDLY STATED TO THE CHINESE IN BOTH PUBLIC AND PRIVATE SETTINGS, INCLUDING THE NOVEMBER VISIT OF UNDERSECRETARY ARMACOST. WE BELIEVE THAT CENTRAL GOVERNMENT OFFICIALS HAVE ACCEPTED OUR ASSURANCES ABOUT CONTINUED LONG-TERM U.S. SUPPORT FOR CHINA'S MODERNIZATION AND NO CHANGE IN EXISTING EXPORT LICENSING PROCEDURES, AND OUR EXPLANATIONS THAT THE PRESENCE OF CHINESE-MADE WEAPONS IN THE GULF HAS SERIOUSLY UNDERMINED POLITICAL SUPPORT IN CONGRESS AND THE ADMINISTRATION FOR FURTHER RELAXATION OF RESTRICTIONS ON TECHNOLOGY TRANSFER TO CHINA. FOR PRC POLICYMAKERS, THE LINKAGE BETWEEN TECH TRANSFER AND ARMS SALES IS EXPLICIT AND UNAMBIGUOUS. CHINA STILL MUST TAKE A NUMBER OF RELATED ACTIONS BEFORE

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WE WOULD BE PREPARED TO PUT THE LIBERALIZATION PROCESS BACK ON TRACK.

4. IN THE MEANTIME, HOWEVER, WE ARE CONCERNED THAT OUR POLICY ON THIS ISSUE IS NOT FULLY UNDERSTOOD BY WORKING-LEVEL BUREAUCRATS AND PURCHASING AGENTS FOR CHINESE END-USERS, NOR BY U.S. EXPORTERS, AND IS HAVING THE UNINTENDED EFFECT OF HAMPERING THE COMPETITIVENESS OF U.S. FIRMS HERE. SPECIFICALLY, U.S. FIRMS REPORT THAT SOME CHINESE BUYERS ARE INCREASINGLY RELUCTANT TO CONSIDER U.S. OFFERS BECAUSE OF FEARS THAT THE DECISION TO POSTPONE FURTHER LIBERALIZATION WILL MEAN IN PRACTICE A REDUCTION IN THE LEVEL OF TECHNOLOGY THAT THE U.S. IS WILLING TO SELL TO CHINA. IN ONE NOTABLE RECENT EXAMPLE, THE CHINA NATIONAL TECHNOLOGY IMPORT CORPORATION (CNTIC) OVERRULED A CHINESE END-USER'S DECISION TO BUY A COMPUTER SYSTEM FROM HEWLETT-PACKARD AND AWARDED THE CONTRACT INSTEAD TO A FRENCH FIRM, BULL. CNTIC ARGUED THAT IN LIGHT OF THE U.S. REACTION TO SILKWORM MISSILES IN THE GULF, HP WOULD BE UNABLE TO OBTAIN THE LICENSE WITHIN THE TIME ALLOWED, EVEN THOUGH HP HAD PREVIOUSLY OBTAINED A LICENSE FOR SIMILAR EQUIPMENT SOLD TO CNTIC. HP BELIEVES THAT ITS FRENCH COMPETITOR PLAYED ON CHINESE CONCERNS ABOUT U.S. POLICY TO TAKE THE CONTRACT AWAY FROM HP. DESPITE ARGUMENTS THAT POSTPONEMENT OF LIBERALIZATION FOR CHINA HAD NOT AFFECTED CURRENT LICENSING POLICY, HP WAS UNABLE TO CONVINCE CNTIC THAT IT WOULD BE ABLE TO OBTAIN AN EXPORT LICENSE.

5. SOME CHINESE BUYERS WHO UNDERSTAND OUR LIBERALIZATION POLICY MAY CYNICALLY USE THE RUMOR OF U.S. ROLLBACK TO EXTRACT CONCESSIONS FROM U.S. SUPPLIERS OR AS AN EXCUSE TO TURN TO OTHER SUPPLIERS. MANY U.S. FIRMS HERE, HOWEVER, FEEL MISUNDERSTANDING OF THE INTENT AND SCOPE OF U.S. POLICY IS A MORE SERIOUS AND WIDESPREAD PROBLEM AND THAT MORE NEEDS TO BE DONE TO MAKE U.S. POLICY UNAMBIGUOUSLY CLEAR TO THOSE MAKING PURCHASING DECISIONS. WHILE U.S. BUSINESSMEN RECOGNIZE THE REASONS BEHIND THE LIBERALIZATION POSTPONEMENT, THEY FEAR FURTHER SLIPPAGE IN THEIR COMPETITIVENESS UNLESS THEIR CHINESE COUNTERPARTS ARE PRESENTED WITH EVIDENCE THAT LICENSING PROCEDURES AND APPROVAL LIMITS HAVE NOT REGRESSED. ROGER SULLIVAN, CHAIRMAN OF THE NATIONAL COUNCIL ON U.S.-CHINA TRADE BROUGHT THIS ISSUE TO AMBASSADOR LORD'S ATTENTION IN A RECENT LETTER, AND THE BEIJING OFFICE OF THE NSCST HAS EXPRESSED TO THE EMBASSY ITS CONCERN ON BEHALF OF U.S. BUSINESS.

6. EMBASSY COMMERCIAL AND ECONOMIC OFFICERS HAVE VOLUNTEERED TO CALL ON CHINESE OFFICIALS AS NECESSARY TO SET THE RECORD STRAIGHT, BUT THIS EFFORT IS RESTRICTED BY TIME AND THE LARGE NUMBER OF PRC OFFICIALS INVOLVED. TO PROVIDE MORE EFFECTIVE MEANS FOR U.S. BUSINESSMEN TO REBUT FALSE STATEMENTS ON U.S. POLICY, WE BELIEVE A RESTATEMENT OF THAT POLICY, IN THE FORM OF A BACKGROUNDER BASED ON PREVIOUSLY APPROVED STATEMENTS AND PRESS GUIDANCE, WOULD BE USEFUL. WHILE EMPHASIZING ONCE AGAIN THAT LIBERALIZATION IS CONTINGENT UPON PROGRESS IN CURBING ARMS SHIPMENTS TO IRAN, WE CAN OFFER WRITTEN EVIDENCE THAT THERE HAS BEEN NO REDUCTION IN THE LEVEL OF TECHNOLOGY APPROVED FOR SALE TO CHINA. THE BACKGROUNDER WOULD BE MADE AVAILABLE TO U.S. COMPANIES IN THE SAME MANNER THAT WE ACTIVELY PROVIDE INFORMATION ON OTHER TOPICS OF INTEREST. IT WOULD NOT BE DISTRIBUTED DIRECTLY TO PRC OFFICIALS BY THE EMBASSY. NATURALLY, IF ASKED, WE WILL EMPHASIZE THAT THE BACKGROUNDER REPRESENTS NO CHANGE IN CURRENT U.S. POLICY. OUR

DATE: 1/6/88

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PROPOSED TEXT, TO BE ISSUED ON EMBASSY LETTERHEAD,
APPEARS BELOW.

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7. BEGIN TEXT.

U.S. GOVERNMENT POLICY ON EXPORT CONTROLS FOR CHINA

SUBSTANTIAL PROGRESS HAS BEEN MADE SINCE 1983 IN
LIBERALIZING U.S. RESTRICTIONS ON ADVANCED TECHNOLOGY
EXPORTS TO CHINA. THE RANGE OF TECHNOLOGY SUBJECT TO
LIBERALIZED TREATMENT HAS BEEN EXPANDED, WHILE LICENSE
PROCESSING TIMES HAVE BEEN SUBSTANTIALLY REDUCED. AS
A RESULT, U.S. EXPORT LICENSE APPROVALS FOR CHINA MORE
THAN TRIPLED BETWEEN 1983 AND 1986.

RECENTLY, DUE TO AN INCREASE IN TENSIONS IN THE PERSIAN
GULF RESULTING FROM IRAN'S USE OF CHINESE-ORIGIN
WEAPONS AGAINST NEUTRAL SHIPPING AND OTHER TARGETS,
THE U.S. DECIDED TO POSTPONE REVIEW OF FURTHER EXPORT
CONTROL LIBERALIZATION FOR CHINA. AS PRESIDENT
REAGAN'S PREVIOUS STATEMENTS AND OUR PAST RECORD
DEMONSTRATE, THE U.S. IS COMMITTED TO THE LIBERALIZATION
PROCESS, AND WE EXPECT TO PROCEED WITH FURTHER EASING
OF RESTRICTIONS AT AN APPROPRIATE TIME. THE PACE AND
TIMING OF LIBERALIZATION WILL VARY, AS IT HAS IN THE
PAST.

IN THE MEANTIME, THE U.S. DOES NOT INTEND TO REDUCE THE
VOLUME OR TECHNOLOGICAL LEVEL OF PRODUCTS AVAILABLE TO
CHINA UNDER EXISTING LICENSING PROCEDURES. MEASURES
ALREADY ADOPTED TO LIBERALIZE REGULATIONS GOVERNING
U.S. EXPORT CONTROLS WILL NOT BE AFFECTED BY OUR RECENT
DECISION TO POSTPONE FURTHER LIBERALIZATION.

END TEXT.

8. ACTION REQUESTED: PLEASE PROVIDE DEPARTMENT
CONCURRENCE WITH THE CONTENT OF THE PROPOSED BACK-
GROUNDER AND WITH EMBASSY REQUEST TO ISSUE THE BACK-
GROUNDER TO U.S. COMPANIES IN CHINA. ASSUMING
DEPARTMENT CONCURRENCE, WE SUGGEST THE DEPARTMENT
MAY WISH TO MAKE THIS STATEMENT AVAILABLE TO ROGER
SULLIVAN AT THE NATIONAL COUNCIL ON U.S.-CHINA TRADE.
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